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RUEATRS/DEPT OF TREASURY WASHDC
RUEKJCS/Joint STAFF WASHDC
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RHEHNSC/NSC WASHDC 0269
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RUEAIIA/CIA WASHDC
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SUBJECT: KAZAKHSTAN: WORLD BANK COUNTRY MANAGER DISCUSSES
ECONOMIC SITUATION, BOTA FOUNDATION

REF: ASTANA 2070

¶1. (U) Sensitive but unclassified. Not for Internet distribution.

¶2. (SBU) SUMMARY. During an October 15 introductory meeting with the Ambassador, World Bank Country Manager for Kazakhstan Sergei Shatalov provided his views on the state of the Kazakhstani economy, discussed the government's efforts to deal with the global financial crisis, and gave an update on the activities of the Bota Foundation. END SUMMARY.

ECONOMIC OVERVIEW

¶3. (SBU) Shatalov told the Ambassador that economic growth in Kazakhstan has been down for the last three quarters. With the exceptions of the Atyrau and Aktau regions -- the heart of Kazakhstan's hydrocarbons sector -- growth has actually been flat in the country as a whole. According to Shatalov, Chinese demand for raw materials is shrinking as China switches to domestic producers, which is having a significant impact on steel production in Kazakhstan. (NOTE: This was evidenced by the October 3 layoffs of over 4000 steel workers from the Temirtau steelworks owned by ArcelorMittal. END NOTE.)

¶4. (SBU) Shatalov explained that the grain harvest is down significantly this year, and maintained that grain exports will not exceed 3 million tons, as a result of which Kazakhstan will not reach the ranks of one of the world's top five wheat exporters. (NOTE: The government maintains that overall grain exports will be between 5.5 and 6 million tons. END NOTE.) The construction sector has visibly declined throughout Kazakhstan, particularly in Astana, where most of

what is currently under development is driven by government spending. There remains almost no foreign direct investment in the construction sector. On a more positive note, Shatalov said that Shymkent appears to be benefiting from significant private sector investments in various sectors of its economy.

BANKING SECTOR NOT YET IN THE CLEAR

15. (SBU) Shatalov painted a picture of the banking sector not nearly as rosy as that presented to the public by Kazakhstani financial authorities. According to Shatalov, the credit crisis in the construction sector has been accompanied by a significant drop in real estate values -- by up to 50% in Almaty -- leaving many banks with a very significant burden of debt, and very little collateral. Forty percent of the balance sheet of the Kazakhstani banking sector is comprised of debt and mortgages. This ratio holds true for Kazakhstan's two largest banks, Bank Turan Alem and KazKommertsBank.

RECOVERY EFFORTS QUESTIONABLE

16. (SBU) When asked about the prospects for Kazakhstan's recovery from the global financial crisis, Shatalov noted that the government had allocated \$10 billion from the National (Oil) Fund on October 13 as part of a stabilization package. This allocation is in addition to the \$4 billion made available last year from other reserves to support the construction sector, of which \$2 billion has been transferred to banks under very strict lending conditions. Shatalov questioned the government's decision to merge the Samruk

ASTANA 00002095 002 OF 003

state assets holding company and the Kazyna Sustainable Development Fund into the Samruk-Kazyna National Welfare Fund. He termed Samruk-Kazyna a "super monster" and said the relevance of the merger to dealing with the financial crisis was unclear (see reftel). He did, however, praise the recent creation of a stressed assets fund to buy up bad loans from banks, noting that after consultations with the World Bank, Kazakhstani financial authorities seem to be closely studying the case of the Resolution Trust Corporation (RTC), which liquidated the assets of failed savings and loan institutions in the United States in the late 1980s and early 1990s. Shatalov maintained that overall, there needs to be greater transparency with respect to the assets of Kazakhstan's banking sector -- which are estimated to be \$120 billion, roughly the equivalent of the country's Gross Domestic Product.

BOTA FOUNDATION OPEN FOR BUSINESS

17. (SBU) Shatalov gave the Ambassador a detailed update on the Bota Foundation, which was established by the United States, Kazakhstan, and Switzerland to disburse for humanitarian purposes \$84 million in frozen bank funds linked to the James Giffen bribery case. He described Bota as "at a turning point." After three months of intensive work, Kazakhstan's Ministry of Justice (MOJ) and the U.S. Department of Justice (DOJ) finally reached agreement on changes to several of Bota's statutory documents. The Bota MOU between the three country partners was also renegotiated.

Shatalov called the MOJ's work exemplary, specifically praising Deputy Justice Minister Marat Beketayev, who managed to get the foundation registered in just one day. He half-jokingly noted that making such speedy registration routine would do "worlds of good" for Kazakhstan's ranking in the World Bank's annual "Doing Business" report.

18. (SBU) Shatalov explained that at an October 7 meeting, Bota's Board of Trustees selected IREX/Save the Children as the winning bidder to be the foundation's program manager. This decision is subject to approval by the three governments, as well as the successful conclusion of contract negotiations with IREX/Save the Children by October 31.

Shatalov praised the work to date of the Board (of which former U.S. Ambassador to Kazakhstan John Ordway is a member). He said that the Kazakhstani trustees have been diligent, independent, and proactive, and "dead set" on the efficient use of Bota's funds.

¶9. (SBU) Shatalov said that Bota anticipates launching its programmatic activities in November. Assistance will be targeted to specific regions, which will be selected based on rural poverty rates. Shatalov noted, however, that existing Kazakhstani data on poverty has proven unreliable. To better address this issue, the Kazakhstani government recently commissioned the World Bank to conduct a standardized poverty study that will greatly assist in the identification of the regions most in need of assistance, as well as provide a basis for the comparison of poverty statistics across the Central Asia region. In the meantime, a World Bank specialist is "roving the countryside" to identify at risk groups in need of Bota Foundation attention.

¶10. (SBU) Shatalov emphasized that the World Bank's primary work on Bota is to define an efficient delivery mechanism for the assistance. The role of the Kazakhstani government will, of course, be limited to the provision of material

ASTANA 00002095 003 OF 003

support, such as office space, not to exceed the mandated 5-year program period. The World Bank hopes, however, that many of the expected Bota Foundation regional offices will remain open after the 5-year period via private and corporate contributions, thereby fulfilling the second mandate of the foundation: to nurture a philanthropic culture in Kazakhstan. According to Shatalov, the Bota Foundation will serve as a model for similar opportunities identified in Chad and Cameroon.

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